

Message Text

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SUBJECT: NEW POLISH TAX REGULATIONS

REF: (A) WARSAW 4619; (B) WARSAW 4942; (C) WARSAW 4988;
(D) TREASURY CABLE OF SEPT. 27, 1973

PASS TREASURY FOR DEPUTY TO THE ASSISTANT SECRETARY
(INTERNATIONAL TAX POLICY) NATHAN GORDON

PASS COMMERCE FOR BEWT

1. NEW POLISH REGULATIONS ON TAXATION OF WESTERN FIRMS
IN POLAND ARE NOW IN STAGE OF FINAL INTERMINISTERIAL
CLEARANCE. EMBASSY HAS NOT YET BEEN ABLE TO OBTAIN COPY
OF REGULATIONS, BUT MINISTRY OF FINANCE HAS PROMISED TO
PROVIDE COPY BEFORE DEPARTURE OF POLISH TAX NEGOTIATORS
FOR WASHINGTON ON NOVEMBER 16. INFORMATION BELOW IS BASED
ON SERIES OF CONVERSATIONS WITH MINISTRY OF FINANCE TAX
SPECIALISTS.

2. AS ALREADY REPORTED, COMMERCIAL AND TECHNICAL OFFICES
WILL RECEIVE ESSENTIALLY SAME TREATMENT UNDER NEW REGULA-
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TIONS. ALL COMMERCIAL ACTIVITIES OF THESE OFFICES WILL
BE SUBJECT TO "INCOME TAX" AT MAXIMUM RATE OF 50 PERCENT.
INCOME IS CONSIDERED TO EQUAL 5 PERCENT OF SALES, EXCLUDING FREIGHT
AND INSURANCE. THUS TECHNICAL AND COMMERCIAL OFFICES WILL PAY

2.5 PERCENT OF SALES TO POLISH STATE IN TAXES, WITH EXCEPTIONS NOTED IN PARAS 3 AND 4 BELOW.

3. IN CASES IN WHICH A PARENT COMPANY CAN PROVE, THROUGH ITS FINANCIAL STATEMENT, THAT ITS OVERALL WORLDWIDE PROFITS WERE LESS THAN 5 PERCENT OF SALES (EXCLUDING FREIGHT AND INSURANCE), THE PROVEN LOWER PERCENTAGE WILL BE USED TO DETERMINE THE TAXABLE INCOME OF THE BRANCH OFFICE IN POLAND.

4. A TECHNICAL OFFICE WILL BE EXEMPT FROM TAX ON INCOME DERIVED FROM SALES ON WHICH A COMMISSION IS PAID TO A POLISH COMMERCIAL AGENCY FIRM.

5. WHEN IT WAS SUGGESTED THAT THE POLISH TAX MIGHT BE CONSIDERED BY U.S. AUTHORITIES TO BE A TAX ON SALES RATHER THAN ON INCOME, MINISTRY OFFICIALS REPLIED THAT POLISH WILLINGNESS TO ACCEPT (UNDER CIRCUMSTANCES DESCRIBED IN PARA 3) A TAX BASE LESS THAN 5 PERCENT OF SALES DEMONSTRATES THAT THE TAX IS APPLIED TO PROFIT. WHEN ASKED WHETHER THE TAX WOULD STILL BE LEVIED IN CASES IN WHICH IT COULD BE DEMONSTRATED THAT THE BRANCH OFFICE IN POLAND, ALTHOUGH NOT THE PARENT COMPANY, OPERATED AT A LOSS, MINISTRY OFFICIALS REPLIED THAT THE SITUATION WAS NOT COVERED IN REGULATIONS, BUT THAT SUCH PROBLEMS COULD BE DEALT WITH EXCEPTIONALLY OUTSIDE OF THE REGULATIONS.

6. TAX LIABILITY OF U.S. FIRMS ENGAGED IN TURNKEY PROJECTS WAS DISCUSSED WITH MINISTRY OFFICIALS ON NOVEMBER 7 BY STANLEY HAYNES OF SWINDELL-DRESSLER DIVISION OF PULLMAN. SWINDELL-DRESSLER CONCLUDED A CONTRACT EARLIER THIS YEAR VALUED AT ABOUT \$40 MILLION FOR TURNKEY CONSTRUCTION OF A FOUNDRY IN POLAND AND IS SUBMITTING PROPOSALS FOR AN ADDITIONAL \$200 MILLION WORTH OF TURNKEY CONTRACTS. EMBASSY OFFICER KOPP WAS PRESENT DURING HAYNES' TALK WITH MINISTRY OFFICIALS. (PULLMAN INCORPORATED SUBMITTED APPLICATION ON NOVEMBER 6 FOR A LICENSE TO OPEN A TECHNICAL OFFICE IN POLAND, ALTHOUGH HAYNES NOW HAS SERIOUS QUESTIONS ABOUT THIS LIMITED OFFICIAL USE
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STEP IN LIGHT OF UNANSWERED TAX QUESTIONS.)

7. MINISTRY OFFICIALS NOTED THAT CONSTRUCTION ACTIVITY WOULD NOT BE SUBJECT TO THE SAME REGULATIONS AS COMMERCIAL ACTIVITY. EXEMPTION OF US FIRMS ENGAGED IN CONSTRUCTION ACTIVITY IN POLAND FROM POLISH TAXES WAS FORESEEN UNDER THE CONVENTION FOR AVOIDANCE OF DOUBLE TAXATION CURRENTLY UNDER NEGOTIATION, BUT THE PERIOD DURING WHICH THE FIRM MUST BE ACTIVE TO QUALIFY FOR EXEMPTION WAS A POINT AT ISSUE, WITH THE U.S. SIDE PROPOSING 36 MONTHS AND THE POLISH SIDE 12 MONTHS, MINISTRY OFFICIALS SAID. PROFIT ON CONSTRUCTION ACTIVITY IS CONSIDERED TO BE 10 PERCENT OF VALUE

OF THE CONTRACT, TAXABLE AT 50 PERCENT. AGAIN, IF THE PARENT COMPANY (IN THIS CASE NOT SWINDELL-DRESSLER BUT PULLMAN) CAN DEMONSTRATE THAT ITS PROFITS ARE BELOW 10 PERCENT, THE LOWER FIGURE WILL APPLY.

8. ALTERNATIVELY, MINISTRY OFFICIALS SAID, POLAND WOULD ACCEPT A FIGURE BASED ON THE BOOKS FOR A SPECIFIC PROJECT. SWINDELL-DRESSLER REPLIED THAT IT COULD NOT REVEAL ITS BOOKS ON A POLISH PROJECT TO THE POLISH GOVERNMENT WITHOUT JEOPARDIZING ITS NEGOTIATING POSITION FOR FUTURE CONTRACTS, THE MORE SO BECAUSE POLISH FOREIGN TRADE COMPANIES WILL NOT LET TURNKEY PROJECTS ON A COST-PLUS BASIS.

9. RETENTION OF A POLISH COMMERCIAL AGENT WOULD NOT AFFECT THE LIABILITY OF A COMPANY ENGAGED IN CONSTRUCTION RATHER THAN COMMERCIAL ACTIVITIES, ACCORDING TO MINISTRY OFFICIALS.

10. SWINDELL-DRESSLER'S PRESENT CONTRACT CALLS FOR THE POLISH PARTNER TO ASSUME FULL RESPONSIBILITY FOR S-D'S TAXES DUE IN POLAND AND FOR S-D TO ASSUME RESPONSIBILITY FOR THE TAXES OF THE POLISH PARTNER DUE IN THE UNITED STATES. THIS ARRANGEMENT WILL BE UNAFFECTED BY THE NEW REGULATIONS, WHICH WILL NOT APPLY RETROACTIVELY, MINISTRY OFFICIALS SAID. S-D HAS DECIDED IN ANY CASE NOT TO SIGN FURTHER CONTRACTS HERE UNTIL ITS TAX SITUATION IS CLARIFIED. UNRESOLVED ISSUES INCLUDE TAXATION ON FUNDS SPENT IN POLAND (FOR LABOR, BUILDING MATERIALS, ETC.), LIMITED OFFICIAL USE
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AND TAXATION ON PAYMENTS TO S-D IN POLISH CURRENCY.

11. BEGIN COMMENT: ALTHOUGH THE EMBASSY CLAIMS NO EXPERTISE IN U.S. TAX LAW, THE POLISH TAX ON COMMERCIAL AND TECHNICAL OFFICES, AS GOP APPARENTLY INTENDS TO APPLY IT, DOES NOT SEEM TO US TO BE COMPATIBLE WITH THE U.S. CONCEPTION OF TAX ON INCOME. THE UNWILLINGNESS OF POLISH AUTHORITIES TO ACCEPT THE VALIDITY OF THE BOOKS OF THE POLISH BRANCH OFFICE OF THE U.S. FIRM LIES AT THE HEART OF THE PROBLEM. THE PRESENT POSITION APPEARS TO BE A RETREAT FROM THAT EXPRESSED DURING JULY TAX TALKS IN WARSAW. (IN THIS REGARD ALSO SEE REF A CONCERNING DOW CHEMICAL'S SITUATION). IT SHOULD BE NOTED THAT POLISH OFFICES IN THE UNITED STATES ARE SUBJECT TO TAX ON THEIR PROFITS AS SHOWN IN THEIR OWN ACCOUNTING, NOT AS ESTABLISHED BY AN ARBITRARY PERCENTAGE OR CALCULATED ACCORDING TO THE PROFITS OF THE PARENT COMPANY. SINCE SALES TAXES ARE NOT COVERED IN THE DRAFT CONVENTION ON AVOIDANCE OF DOUBLE TAXATION AND CANNOT BE CREDITED AGAINST TAXES DUE IN THE UNITED STATES, THE NEW POLISH REGULATIONS MAY PRODUCE A

SITUATION IN WHICH IT IS MORE PROFITABLE FOR A U.S. FIRM
TO OPERATE THE POLISH MARKET FROM OUTSIDE POLAND. DURING
THE THIRD SESSION OF THE JOINT U.S.-POLISH TRADE COMMISSION,
THE U.S. DELEGATION POINTED OUT THAT POLISH TAX LAWS
SHOULD NOT DILUTE THE EFFORTS OF THE POLISH GOVERNMENT
TO ATTRACT PERMANENT REPRESENTATION BY U.S.
FIRMS IN POLAND AND TO EXPAND AND INTESIFY
U.S.-POLISH TRADE AND INDUSTRIAL COOPERATION RELATIONS.

12. THE MATTER OF TURNKEY PROJECTS IS UNCLEAR AND
UNRESOLVED. IT WAS APPARENT FROM HAYNES' TALK WITH
MINISTRY OF FINANCE OFFICIALS THAT THE MINISTRY HAS
NOT YET GIVEN SERIOUS THOUGHT TO THIS ISSUE AND IS
UNFAMILIAR WITH THE NATURE OF TURNKEY OPERATIONS.
SWINDELL-DRESSLER'S GENERAL COUNSEL JOHN MCLANE HOPES
TO MEET WITH GORDON OF TREASURY WITHIN NEXT FEW DAYS AND
THEN VISIT WARSAW NOVEMBER 14-15 TO MEET WITH MINISTRY
OF FINANCE. THESE FURTHER TALKS WITH MINISTRY MAY SHED
SOME LIGHT ON THIS PROBLEM BEFORE DEPARTURE OF POLISH
TAX DELEGATION TO WASHINGTON.

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13. IN VIEW OF IMPORTANCE OF OVERALL TAX SITUATION FOR
U.S. COMPANIES CURRENTLY ENGAGED IN BUSINESS HERE,
TOGETHER WITH NUMEROUS AREAS OF NEW POLISH LAW WHICH
REMAIN TO BE CLARIFIED, EMBASSY IS RECOMMENDING IN SEPTEL
THAT EMBOFF KOPP BE ASSIGNED TO THE U.S. DELEGATION FOR
SECOND ROUND OF BILATERAL TAX CONVENTION NEGOTIATIONS
SCHEUDLED TO BEGIN AT WASHINGTON ON NOVEMBER 19.

END COMMENT.

DAVIES

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